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WORLD INVESTMENT REPORT 1996

Karl SAUVANT, Chief of the Research and Policy Analysis Branch of UNCTAD's Division on Transnational Corporations and Investment, discusses the impact of foreign direct investment (FDI) on the economic growth and development of developed and developing nations. The rapid increase in foreign direct investment has complicated the relationship between world trade and investment. UNCTAD plays a key role in providing research on investment issues and assists developing countries to prepare for negotiations on such matters. Mr. Sauvant indicates that during the period covered by the report, total FDI flow into developing countries rose 15 per cent, totalling US $100 billion.

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ANNOUNCER: From United Nations Headquarters in New York, this is **World Chronicle**, an unedited interview programme about major global issues. Here now to introduce our guest is the host of today's **World Chronicle**.

LITTLEJOHNS: I'm Michael Littlejohns, and this is **World Chronicle**.

Competitive pressures, new technologies, privatization and national Government policies are the main factors behind the rapid increase in foreign direct investment. These are among the findings of a report on world investment [World Investment Report 1996] recently published by UNCTAD, the United Nations Conference on Trade and Development. What will this increase in foreign direct investment mean to international trade, and what will be its impact on the economic growth and welfare of developed and, in particular, developing countries?

With us today is the team leader who prepared the Report. He is Karl Sauvant, Chief of the Research and Policy Analysis Branch of UNCTAD's Division on Transnational Corporations and Investment. Joining me to talk with Mr. Sauvant are James Bone of *The Times* of London and Afsane Bassir Pour of *Le Monde*.

Mr. Sauvant, welcome to World Chronicle. Mr. Sauvant, I had the pleasure of attending the first meeting of UNCTAD in 1964 in Geneva, so I know what it's all about, but our listeners and television audience probably don't have much idea about UNCTAD. Would you just give us a brief outline of what UNCTAD exists to do?

SAUVANT: Well, UNCTAD is, within the UN system, the organization that is responsible for all issues relating to development, and it looks at world economic issues from the developmental angle. As you mentioned, UNCTAD was established in 1964. It has had a number of conferences of all the participating countries, all the member countries, which are about 188. And the last of these conferences—the latest of these conferences, not the last, I hope—the latest of these conferences was in Midrand in South Africa earlier this year. And it actually initiated a reform process, both at the intergovernmental level and at the secretarial level, under the leadership of our new Secretary-General, Mr. Rubens Ricupero from Brazil, which focused the work of UNCTAD very much on the area of trade and investment as well as services infrastructure, and which has streamlined the machinery, the intergovernmental machinery, accordingly. In fact, at the end of the conference all countries were very satisfied with this reform process, and it is being held up as a model of reform within the UN system.

LITTLEJOHNS: As I recall, the United States was not all that enthusiastic about UNCTAD when it was set up, and I remember George Ball, who was the Under Secretary of State at the time, and he—in fact, I was on the same plane, we travelled together to Geneva,

and he was a little negative about it at that time. And more recently the United States has even talked about disbanding UNCTAD. What is the situation now?

SAUVANT: Well, the situation has changed drastically since UNCTAD IX. This is reflected, for instance, in the communiqué of the Group of 7 at the Lyons Summit in 1996, in which actually UNCTAD was held up as a model of reform within the UN system. So I think UNCTAD is working with the support of all groups of countries, which of course gives it a better possibility to influence international discussions in the area of development.

BONE: Mr. Sauvant, though, they've just set up the World Trade Organization. Doesn't UNCTAD duplicate those functions?

SAUVANT: That issue was raised, of course, by a number of observers, but I think the question has been pretty much put to rest, also since UNCTAD IX earlier this year. And basically the division of labour which has been agreed upon is that UNCTAD is very much a deliberative body, which undertakes policy research and consensus-building on issues concerning development, with of course particular attention being paid to developing countries, while the WTO is really a body in which negotiations take place and in which agreements are being implemented.

BONE: Isn't there an ideological difference between the two? I mean, the World Trade Organization is the result of the GATT negotiations and is basically a free trade organization, whereas UNCTAD has traditionally favoured things like commodity price stabilization. Isn't there a difference of philosophy between the two organizations?

SAUVANT: I don't think that there is a difference in philosophy. Obviously UNCTAD is paying a bit more attention to, or focuses attention on, the developmental aspects in terms of its analysis and its consensus-building, and brings this perspective into the international negotiations. But I can tell you—for instance, in the area in which I have been involved, in issues related to foreign direct investment—that in discussion with the WTO the cooperation has been quite smooth. We have had a number of events, informal events with the participation of people from the WTO, both the secretariat as well as the diplomatic community, which were judged as very useful both by the WTO and by UNCTAD.

BASSIR POUR: As Michael mentioned and you said yourself, we're seeing record foreign direct investments. Could you explain what has led to this, what are the trends?

SAUVANT: We see, I think, two trends which are noteworthy. The first one is a surface trend, which is that you have seen since the mid-1980s a substantial increase of investment flows worldwide. At the beginning of the 80s, worldwide investment flows were approximately $40 billion. Last year, 1995, they were $315 billion, with investment flows to developing countries alone of $100 billion, meaning two and a half times the total world flow of investment of the early 80s. But that is sort of the annual change. What I think is more

interesting, in a sense, is the underlying change, and the underlying change is that these investment flows are, of course, not perishable; they add to an existing stock of foreign direct investment; and as a result you have now a stock which is worth close to $3 trillion, generating sales worth $6 trillion, higher than world exports, and giving rise—and that's a structural change—giving rise to, or beginning to give rise to, an integrated international production system that spans national boundaries.

BONE: People—well, at the United Nations—are always talking these days about globalization. How do you see globalization? How large is foreign direct investment going to become? What are the implications of globalization, so-called?

SAUVANT: Globalization of course is a broad process which involves financial transactions, involves culture, involves travel, and basically all transactions in our daily life. Foreign direct investment involving the production of goods and services in a sense is the productive core of the globalization process because it involves the establishment of cross-border production systems—for instance, if you have a company like Ford, let's say, which has production facilities in several countries, all being integrated with each other into one transnational production and trade network. And I think that's where the inter-relationship between production and trade becomes increasingly interesting, because you can no longer speak about trade separately from production in this case, but rather you have to look at them at the same time.

BONE: One of the questions I have for you is whether actually development is best served by foreign direct investment. I mean, that seems to me the most effective way of improving the lot of people in developing countries. Would you agree with that?

SAUVANT: Well, basically yes. I think one has to look at foreign direct investment really as a package. After all, while we take the capital flow figures in order to measure it, because they are the easiest available, in reality, foreign direct investment is a package that consists of capital, of technology, of organizational practices, of access to markets—in other words, it consists of a number of tangible and intangible assets. And a country which acquires these tangible and intangible assets, of course, in principle can benefit from these assets. And, of course, countries have recognized that, and therefore there is worldwide competition for foreign direct investment. And, of course, a number of countries are also trying—in addition to attracting foreign direct investment, they're trying various policies to make sure that foreign direct investment contributes as much as possible to domestic development.

BASSIR POUR: I'd like to go back to what you said about having reformed the organization, because it did have a reputation even up to the late 80s equal that of

UNESCO at some point. Now, you said that UNCTAD has become a model for reform, and reform is the word these days. How did you reform, and why is it so successful?

SAUVANT: Well, the reform process, of course, was a process which very much involved—was initiated by Governments, but with full cooperation, of course, of the secretariat. And it consisted of, first of all, focusing the activities of the organization and, in the process, streamlining the organization. For instance, the number of divisions in UNCTAD was reduced considerably, reflecting the focus on the areas I mentioned before. The numbers of meetings were reduced, were focused more sharply. So in that sense the reform process was considered successful.

LITTLEJOHNS: Mr. Sauvant, not so very long ago the transnational corporations were demonized in the United Nations. Now they seem to be looked upon as saviours of the developing countries and candidates for sainthood. Why the change in perception in the last two to three years?

SAUVANT: Well, there has been a change in perception for sure, but I don't think it goes in the direction of sainthood. I think the evaluation of the role of transnational corporations as the principal actors undertaking foreign direct investment has been evaluated in the last decade or so in a more realistic manner. Partly that is because countries have come to learn, to understand the contribution that foreign direct investment can make; partly it is because they have developed their own capacities to deal more confidently with transnational corporations. But overall, the principal reason is, of course, that it has been recognized, as we discussed just a moment ago, that transnational corporations and foreign direct investment can contribute a number of assets to the national development effort—in developed and developing countries, mind you, we're not only talking about developing countries—which are very much sought after, and which countries try to attract. And as a result of that, the attitude to the entities undertaking such investment has changed as well.

LITTLEJOHNS: And has the attitude of the transnational corporations changed? I mean, previously the idea was that somehow or other they were so enormous, so wealthy, that they could control the countries where they were operating. Have they sort of backed off now, and are more cooperative with the Governments in the host countries?

SAUVANT: I think there has been a learning process on the part of corporations as well, which, you know, means that companies are more aware of the developmental needs of countries, which has to do with issues like social responsibility and things like that. It is, I think, a mutual understanding which also comes out of the dialogue which in the last 10 or 20 years has developed between companies and Governments, and where UNCTAD, incidentally, is also playing a role, in the sense of, for instance, having roundtables in individual countries and bringing together investors, companies, and Government officials in

order to discuss what are the mutual expectations, what are the contributions that can be made, and how can you jointly maximize the benefits for both.

BONE: One of the things that's brought out in your Report that's new is that there are a growing number of transnational corporations actually based in so-called developing countries. There are some giant corporations now based in Korea or Mexico or something. Can you tell us a little bit about what you found about those?

SAUVANT: Well, that's an interesting development, which perhaps also has contributed towards diffusing the tension which we had in the past. Traditionally, most foreign direct investment, or all foreign direct investment, came from developed countries. Now you see that the picture is beginning to change. Out of the $315 billion of investment flows in 1995, some 14% or so actually originated in developing countries. We have included in the World Investment Report 1996 not only a list of the largest 100 transnational corporations in terms of their foreign assets, all of which are from developed countries, but we also have included a list of the 50 largest transnational corporations from developing countries, where, incidentally, China and the Republic of Korea are leading in terms of having the greatest number of companies in this list. Now, this shows that—and this is, I think, also a result of globalization—that, you know, to the extent that investment and trade regimes are being liberalized everywhere, companies, regardless of whether they are large or small, are being subjected to competition, regardless of whether they are in developed or developing countries, and foreign direct investment simply becomes an additional source of efficiency and competitiveness in that world market. Incidentally, one more little piece of information: in Asia—after all, the most dynamic region—if you look at the nine most important developing countries in Asia, 40% of their investment inflows come from other developing countries in Asia. So for them, other developing countries are already more important foreign investors than the United States, Europe or Japan.

LITTLEJOHNS: This is **World Chronicle**. Our guest is Karl Sauvant, Chief of the Research and Policy Analysis Branch of UNCTAD's Division on Transnational Corporations and Investment.

BASSIR POUR: What are the criteria for investment for these multinational companies? Why do they want to invest in a country, for example? What is it they're looking at?

SAUVANT: You have basically three sets of criteria. One is market-seeking: namely, that enterprises are looking to service local markets, which is particularly important in the services sector, where you don't have the alternative of trading, in other words, exporting to that market. A second reason is resource-seeking. Resource-seeking can be natural resources, but increasingly it is what we call created assets—skills, R&D capacities, and

similar types of activities. A company might invest in the United States, or any other place, in India, in order to have access to talent. And the third type of investment is efficiency-seeking: namely, that by establishing an intra-firm division of labour you increase your overall performance by, for instance, making sure that, or deciding that, a certain part of a product is being produced in one country where there is a particular comparative advantage to produce it, and then assemble it in a second or third country. And often, of course, these motives are all intertwined and increasingly become intertwined, as the issue is no longer whether you should invest abroad or not but rather that you have already established networks; and then the question becomes, you know, where in a particular existing network do you do what. And I think that is part of the new environment which also has led to a new relationship between foreign direct investment and trade.

LITTLEJOHNS: Mr. Sauvant, you mentioned China and the Republic of Korea as developing countries. For me, at any rate, it's a little difficult to regard these two countries as developing. What are the criteria for UNCTAD's designating developed and developing?

SAUVANT: Well, we follow the United Nations criteria as to what country is considered to be in what particular group of countries.

LITTLEJOHNS: Is it a matter of per capita income, or—?

SAUVANT: It's partly a matter of per capita income, but not only. It's a number of other factors. In the case of the Republic of Korea, as you know, the country is considering to join the OECD, but that does not necessarily take it out from the group of developing countries as far as UN purposes are concerned.

BONE: One of the things that comes out strongly in your Report is the amazing place of China. I think that, the way the figures are, a third of all foreign direct investment is into developing countries, and a third of that is into China. What explains the appetite for investment in China?

SAUVANT: I think the principal reason is—there are two, I think, major reasons, and the first reason is that China, until fairly recently, meaning the end of the 80s, was fairly closed. So there was a certain catching-up effect you could observe.

LITTLEJOHNS: Closed to foreign—?

SAUVANT: Closed to foreign direct investment, yes. And secondly, and of course most importantly, it is a very big market, it is a booming market, it is a growing market, and a large growing market is perhaps the single most important determinant for investment.

LITTLEJOHNS: Cheap labour?

SAUVANT: Cheap labour plays a role too, but it's—increasingly the labour factor is really not the most important factor.

BONE: You mention that perhaps there'll be a short—in the short term at least a slight slowing of investment into China. Why is that?

SAUVANT: Well, there are a number of policy factors; it's not really underlying economic factors. One of them is that China, partly with an eye on the WTO, I suspect, is moving towards a policy of national treatment. And that means that foreign affiliates are being treated in the same way as domestic enterprises, with the implication being twofold: one, that certain incentives which were given to foreign affiliates are being phased out; and, secondly, that domestic enterprises which wanted to take advantage of these incentives and therefore exported capital in order to come back into China as foreign capital in order to get the incentives—in other words, round-tripping—would be discouraged. And I think these are factors which certainly will contribute to a slight decline of foreign direct investment in the short term. There's also the fact that the Government seems to feel that the economy is over-heated and wants to slow down economic growth. And there is also the factor that China has become a bit more selective in terms of letting in foreign direct investment—for instance, in the automobile sector it has established certain limitations in order to, in a sense, avoid over-crowding. So all of these factors will probably combine so that, instead of having $38 billion as in 1995, maybe in 1996 it will be a bit less.

BASSIR POUR: What is the bad news that you've come across in your findings in global trends?

SAUVANT: I think the bad news is that, given the principal determinants of foreign direct investment as being large market-size and growth, countries that do not have these conditions do not benefit very much from foreign direct investment. And the result is that foreign direct investment is very skewed. The 10 largest host countries have two-thirds, receive two-thirds of investment. The 100 smallest host countries receive 1%. So many least-developed countries do not receive very much foreign direct investment, although we should also keep in mind that, given their size, the little investment they get can be quite important for their economies. But overall it's clear that the least-developed countries receive considerably less investment than they are seeking.

BONE: So what should a small country do to get investment?

SAUVANT: Well, in a sense it has to do the same things in order to stimulate domestic investment. It has to see to it that it has a stable macroeconomic climate, and in today's world it probably has to have a certain degree of openness, which is particularly important for foreign investors who have a horizon which is larger than that of a small country, so that it might be able to attract export-oriented foreign direct investment, and that is quite possible. For instance, one of the most successful countries in terms of attracting foreign direct investment is Mauritius, not only in terms of becoming a banking centre, but

also in terms of manufacturing and shipping anything from textiles to electronics to the rest of the world. So there are possibilities, but it's not easy, of course.

LITTLEJOHNS: Let's talk a little bit about Africa. You've mentioned Mauritius, which is a member of the Organization of African Unity. Is the problem with Africa the instability, political instability which makes it unattractive for foreign investment?

SAUVANT: Partly. I think clearly in a country which has an unstable political situation, foreign investors are not very much attracted. But not necessarily so. For instance, foreign direct investment in Angola continued even during the civil war because there was oil—

LITTLEJOHNS: Well, that's because—exactly.

SAUVANT: —and there were specific reasons. But overall—

LITTLEJOHNS: And of course minerals.

SAUVANT: And minerals. But overall, you're right. But I think, in the case of Africa, an additional factor comes in, and that's simply an image problem, that companies consider right off Africa as a whole, and do not look country by country or sector by sector as to what are the possibilities for business. Interesting in this context is that if you take United States data and you look at United States foreign direct investment in Africa, you see that US investment in Africa has been consistently more profitable than investment anywhere else in the world except in east Asia. So, in other words, whatever investment there is is quite profitable and consistently so over time. So the message is, you know, look at Africa, I mean, don't write it off, look at it and see whether there are possibilities for you.

LITTLEJOHNS: And why is that? Excuse me just a minute. Why is it so much more profitable?

SAUVANT: Well, it's partly profitable, of course, because, at least in the past, markets were protected, but it's also partly profitable because not too many companies look actually at Africa, therefore there's less competition overall.

BONE: I was struck by your figures on Nigeria, which seems to have by far the largest amount of foreign direct investment of sub-Saharan Africa.

SAUVANT: Yes. It's oil. It's largely oil.

BONE: So it's a distorted figure by oil, really.

BASSIR POUR: In spite of the political situation.

SAUVANT: Yes, yes. It's largely oil. A good part of the investment in Africa is oil. It's Algeria, it's Nigeria and it's Angola. And Egypt, too.

BASSIR POUR: There's a lot of talk about UNCTAD being at the forefront of using modern technology. I understand you're—are you using a lot of modern technology, Internet? And how are you using it?

SAUVANT: Well, we use modern technology in a number of ways. One, using Internet, for instance, in order to disseminate the World Investment Report. I hope it is available as of yesterday. Or at least the Executive Summary. But we are also using modern technology in other projects. For instance, we have a trade point project where countries are linked through an international electronic network in order to explore possibilities. And there are a number of other areas where we try to use modern technology as much as possible.

LITTLEJOHNS: Mr. Sauvant, we have only a few minutes left, a few seconds left, I should say. Afsane mentioned earlier on reform, which of course is the flavour of the month in the United Nations. Is UNCTAD into reform? Are you a leaner, meaner organization than perhaps when you first joined it?

SAUVANT: I think we are certainly moving quite rapidly in that direction. It's not only leaner and meaner, but I think it's also more open, for instance, to civic society. We involve actively the business community, labour, NGOs in our activities, and obviously that enriches our activities and is of benefit to those who get involved in it.

LITTLEJOHNS: Mr. Sauvant, that's all the time we have. Thank you for being with us on this edition of **World Chronicle**. Our guest has been Karl Sauvant, Chief of the Research and Policy Analysis Branch of UNCTAD's Division on Transnational Corporations and Investment. That's quite a mouthful. He was interviewed by James Bone of *The Times* of London and Afsane Bassir Pour of *Le Monde*.

I'm Michael Littlejohns. Thank you for joining us. We invite you to be with us for the next edition of **World Chronicle**.

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